No. 12546.

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

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JACK MAU,

*Appellant,*

*vs.*

PAUL W. SAMPSELL, Trustee in Bankruptcy of the Estate of JACK MAU, Bankrupt,

*Appellee.*

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## BRIEF OF APPELLEE.

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## TABLE OF AUTHORITIES CITED

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## BRIEF OF APPELLEE.

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The issues before this Court in this matter are very simple. Jack Mau, the bankrupt, was engaged in the haberdashery business in Los Angeles. He was buying merchandise extensively on credit and apparently was operating more or less on a shoestring with bankruptcy as the inevitable result. The situation was further complicated by domestic difficulties with his wife and divorce proceedings were pending in the Superior Court. Mau owned a home in Hollywood which was heavily encumbered, the amount of the encumbrance approximating $11,500.00 [Tr. p. 89]. There had been some verbal negotiations between the bank, Mrs. Mau, and the bankrupt with regard to procuring a blanket loan of $12,500.00 from the bank, $11,500.00 of it to constitute a mere renewal of the existing encumbrances thereon and $1,000.00 to be paid over to the bankrupt [Rep. Tr. pp. 89,90].

These transactions had apparently not proceeded beyond the verbal negotiation stage. In fact, the negotiations appear to have been principally with the bankrupt's wife rather than the bankrupt [Tr. p. 90]. Probably because of the bitterness growing out of these domestic troubles, Mrs. Mau refused to go along and no escrow was ever opened.

In the meantime, Mau had a bill with Walbrooke Clothes, Inc., of Trenton, N. J. on which he owed the sum of $730.92 [Tr. p. 22]. Walbrooke Clothes, Inc., was becoming impatient and wrote the bankrupt a letter demanding payment and calling the bankrupt's attention to the fact that the bill was overdue and had not been paid [Tr. p. 22]. Not hearing from the bankrupt, Walbrooke Clothes, Inc. got in touch with its local representative, Ellis Wishnow, and directed him to press the bankrupt for payment of the bill. Wishnow called on the bankrupt at his place of business after two letters had been sent direct from Trenton, N. J. to the bankrupt [Tr. p. 23]. When Wishnow presented his demand personally to the bankrupt for payment of this overdue bill, the bankrupt informed him that he had $12,500.00 in escrow which was to be paid to him and that as soon as the money was released to him he would pay the bill. Wishnow then did the only logical thing under the circumstances, namely, suggested that if that were the case, the thing for him to do would be to write the Credit Manager, Mr. Goldberg, to that effect [Tr. p. 23]. The bankrupt turned the Credit Manager's letter over and in the presence of Mr. Wishnow wrote the false statement complained of, on the back of it, sealed the letter, and gave it to Wishnow to mail [Tr. pp. 91 and 115]. Wishnow commented on the fact that the letter was sealed and no money had been placed therein [Tr. p. 91].

The letter was received by Mr. Goldberg, the Credit Manager, who, believing the bankrupt's lies contained therein, was lulled into a false sense of security and refrained from pressing the claim for payment until it was too late and Mau was in bankruptcy.

Mr. Goldberg's reaction to these falsehoods is demonstrated in his deposition taken during the course of the trial.

At this point, we would backtrack a little bit so as to connect up the deposition which was taken on July 8, 1949, before Ruth D. Budson, Notary Public in Trenton, New Jersey. Specifications of Objection were filed to the bankrupt's discharge and signed by Mr. Early, a young lawyer in the office of the Attorneys for the Trustee, as counsel. The matter was called for trial on May 10, 1949, before Referee Hunt on the Specifications of Objection as drafted by Mr. Early. David Malamed was representing the bankrupt. Believing that Ellis Wishnow was the man who was responsible for the extension or renewal of credit, we relied on him as our witness. It developed at the time of the trial that the extension was actually granted by Mr. Goldberg back in Trenton and that Goldberg's testimony would be necessary to establish reliance thereon [Tr. pp. 48, 49]. It was agreed in open court that Goldberg's deposition could be taken on written interrogatories and the matter was continued [Tr. pp. 49, 50]. A written Stipulation was entered into between Mr. Malamed and the writer of this brief, the original of which apparently had been mislaid, or at least the Referee could not find it, and an executed copy in the hands of counsel was substituted in the record before the Referee therefor [Tr. p. 54]. The matter was adjourned from time to time between May 10th, when Wishnow was examined, and September

9, 1949, when the trial was resumed and completed. In the meantime, Mau had changed attorneys and Messrs. Quittner, Stutman and Shutan became his counsel. An attack was immediately made on the Specifications of Objection to the discharge of the bankrupt as drawn by Mr. Early and an amended objection drawn by the writer was filed [Tr. p. 6]. When the case was called for trial, the deposition of Goldberg which had been taken on written interrogatories previously submitted to Mr. Malamed, was on file and it was subjected to a blizzard of objections by several of counsel for this dishonest bankrupt. A motion to suppress the deposition had been filed and was invoked at the onset of the resumption of the trial [Tr. pp. 51, 52]. The Court's attention was called to the fact that the deposition had been taken pursuant to stipulation [Tr. p. 53], and the question was then raised that it had not been taken in accordance with the provisions of Rule 30-F, 31-B and 32-D [Tr. p. 54]. Counsel for the bankrupt apparently was not as familiar with the deposition as he should have been when he first raised the question that the deposition did not state that the witness was duly sworn [Tr. p. 55]. Counsel was wrong on that. Bankrupt's counsel then fell back on the technicality that there was no certificate that the deposition was a true record of the testimony given by the witness [Tr. pp. 55, 56, 57 and 58]. The Referee then announced that he would sustain that objection to the deposition, but that the objection being purely technical, he would permit the trustee to take it over again and correct the fact that the Notary Public had omitted to certify that it was a true record of the testimony given by the witness, and that he would not permit technicalities to control [Tr. p. 59].

After a recess, counsel for the bankrupt then came in and announced that for the purpose of saving time, but

nevertheless reserving their question of law, they would stipulate that the deposition now before the Court was a retaken deposition which had complied with all of the rules concerning certificates, but notwithstanding this stipulation, reserving their rights to raise the question of the discretion of the Referee in permitting the trustee to take the deposition over again to cure the highly technical question which they had raised [Tr. p. 60]. The deposition was then read in evidence and was greeted with a blizzard of hairsplitting objections to practically every question asked [Tr. pp. 62-73, 75-80, 97-114]. As a result of the objections and arguments made by counsel for the bankrupt, Mau had to be recalled to the stand two or three times and the record is in more or less a state of confusion. However, it is clearly evident from the testimony of the two witnesses, Ellis Wishnow and Isadore Goldberg, supplemented by the examination of the bankrupt as an adverse witness, that the following facts were definitely established: (1) That plaintiff's Exhibit No. 1, the letter in question, was written to the Walbrooke Clothes, Inc., by the bankrupt when Walbrooke Clothes, Inc., was pressing him for payment of his past due obligation [Tr. p. 65]; (2) That this letter contained information and representations regarding the bankrupt's financial condition, namely, that there *was* $12,500.00 in escrow to be released to the bankrupt as soon as he could get the Court Order, and that his case had been postponed for three weeks more [Tr. p. 83]; (3) That there was no escrow to be released to him soon [Tr. p. 83]; (4) That he never paid the bill owing to Walbrooke Clothes, Inc., and that no part of it had been paid up to the date of the hearing on the opposition to discharge [Tr. pp. 84, 85]; (5) That Mau lied not only to the Credit Manager, Goldberg, in the letter, but to the local representative of

Walbrooke Clothes, Inc., when he called on him endeavoring to collect the account [Tr. p. 38]; (6) That Goldberg, upon receipt of the false and untrue letter, relied on the truth of the statements contained therein, and on the strength of them, withheld filing suit against Mau [Tr. pp. 75, 76].

A clearer case could not have been made under Section 14c of the National Bankruptcy Act.

## The Law.

Section 14c of the National Bankruptcy Act insofar as it applies to the case at bar, reads as follows:

> "The court shall grant a discharge, unless satisfied that the bankrupt has (3) obtained money or property on credit, or obtained *an extension or renewal of credit,* by making or publishing or causing to be made or published in any manner whatsoever, a materially false statement in writing *respecting his financial condition.*" (Italics ours.)

Applying the test, not only of law but of reason, logic and sound common sense to this situation, we believe that this court can only reach the same conclusion that was reached by the Referee who saw the witnesses, and particularly the shifty, evasive bankrupt on the stand, and the District Court who reviewed the evidence and the law and was confronted with the same line of abstruse reasoning indulged in here by the bankrupt. The writer of this brief may be somewhat obtuse in his reasoning, or possibly somewhat deficient in his knowledge of the English language as it is spoken in this day and age. Possibly we are so obtuse that we cannot understand why a statement regarding a man's financial condition is not a statement regarding a man's financial condition and why a man

can represent in writing that he has $12,500.00 in escrow which will be released to him very shortly and that the creditor will be paid if he will exercise a little patience, and still not characterize such a written statement as a false statement in writing respecting his financial condition. Possibly, counsel for the bankrupt are too subtle for the writer's unsophisticated mind, but there are a few questions we cannot refrain from asking. There is no dispute that this letter was in writing, written in the bankrupt's own handwriting, sealed in an envelope and delivered to the representative of Walbrooke Clothes, Inc., to forestall pressure on the payment of a past due obligation. Counsel now urge, as they did before the lower Court, that this was not a statement in writing respecting his financial condition such as is meant in Section 14c of the National Bankruptcy Act. If it was not, we would like to know what it was. Was it a statement of his physical condition? Was it a statement of his mental condition? Was it a statement of his marital difficulties, or what? Despite all of the sophistries indulged in by counsel for this dishonest bankrupt, the fact remains and will not down that the bankrupt represented in writing to Walbrooke Clothes, Inc., that *he had $12,500.00 in escrow to be released to him as soon as he got the Court Order;* that his case had been postponed for three weeks more and that the trouble would all be settled in a few weeks [Tr. p. 23]. There was no money; there was no escrow; there was no $12,500.00. If such a statement made to a creditor and intended to be acted upon does not constitute a statement in writing which was materially false and which pertained to the bankrupt's financial condition, then we must confess we do not understand the English language.

The bankrupt has cited a number of cases in his brief, none of which in our opinion, are germane or to the point. At page 9 of his brief, the bankrupt cites two cases: *Johnston v. Johnston,* 63 F. 2d 24, and *In re Morgan,* 267 Fed. 959. *Johnston v. Johnston,* 63 F. 2d 24 in nowise resembles the case at bar. In that case Johnston simply wrote a letter to the Farmers & Merchants Credit Corporation, a creditor, advising them that a relative of his, Vivian D. Johnston, was President and Manager of the Johnston Motor Company, a partnership composed of him and the bankrupt, and had authority to sign any papers in connection with the business. The facts contained in the letter were true, but the signature "James D. Johnston" appended thereto was a forgery, it having been signed by the bankrupt. It did not in any way pertain to the financial condition of the bankrupt. It merely stated that the bankrupt had authority to sign papers on behalf of the partnership and purported to be coming from Col. Johnston, his cousin, which was not true. In affirming an Order over-ruling the objections to the bankrupt's discharge, the Court specifically points out:

> "The letter relied on was plainly not a statement respecting the financial condition of the bankrupt. It related neither to his financial condition nor to that of the partnership of which he was a member, but to his authority to act for the partnership. While its use was reprehensible, it cannot by any sort of interpretation be said to fall within the present language of the act. Even before the statute was amended, not every fraudulent representation would bar discharge. Even the giving of worthless checks or mortgages on property not owned was held not to come within its terms. Robinson v. J. R. Williston & Co., 266 F. 970; *In re* Rea Bros., 251 F. 431; *In re* Hudson, 262 F. 778."

In the *Matter of Morgan,* 267 Fed. 959, cited by counsel on the same page, the bankrupt was a stock broker. The bankrupt had sent out a prospectus pertaining to a stock issue of the Iowa Securities Corporation which was contemplating floating a stock issue through the bankrupt. The prospectus was inflated, but pertained to the soundness of the issuing company, not to the financial condition of the brokerage house. The objecting creditor made no investigation of the securities, but exchanged $4,000.00 worth of bonds in another company for 40 shares of the Iowa Securities Corporation stock. In reversing the Order denying the discharge, the Circuit Court of Appeals for the Second Circuit, speaking through Judge Manton, said:

> "A discharge in bankruptcy is refused when the bankrupt has made false written statements as to his financial standing and thereby obtains money or property from anyone relying on the statement. Firestone v. Harvey (C. C. A., 6th Cir.), 174 Fed. 574; *In re* Bleyer (C. C. A., 2d Cir.), 215 Fed. 896."

Inasmuch as this prospectus did not relate to the financial condition of the bankrupt stock brokerage house, even though it was false, the discharge necessarily had to be granted. In the case at bar, there was a direct representation on the part of the bankrupt that he had among his assets $12,500.00 in escrow to be released very shortly.

On page 10 of his brief, the bankrupt cites *In re Current,* 63 F. 2d 640. This case from the Seventh Circuit is likewise nowise in point. In the *Current* case, the bankrupt apparently conspired with the cashier of the Illiana State Bank at State Line, Indiana, to negotiate a forged paper. In the first instance, he borrowed $2,000.00 on a note co-signed by his brother and his son. When the note

matured, a renewal note was prepared, to be signed by the bankrupt and his brother. Appellant forged his brother's name to the note. The cashier defaulted and the bank closed. The Court of Appeals reversed the Order denying the bankrupt his discharge, on the sole ground that the promissory note was not a false statement in writing respecting his financial condition. A blind person could see that!

We cannot see where *Levy v. Industrial Finance Corporation, et al.,* 276 U. S. 281 lends any aid or comfort to appellant. It merely points out that the amendment of May 27, 1926, changed the wording of Section 14 of the National Bankruptcy Act from:

> "obtained money or property or credit upon a materially false statement in writing made by him to any person or his representative for the purpose of obtaining credit from such person"

to read:

> "A materially false statement * * * respecting his financial condition."

It is true as Justice Holmes said, it served to limit the bars to his discharge more narrowly and by indirection to favor the defendant's position by a change of words, but in what way that statement can be said to help this bankrupt, is beyond our comprehension, because we have here a statement in writing respecting the bankrupt's financial condition to the extent *of $12,500.00.*

*Dave Rauch v. Manchester Smith Company, Inc.,* 240 Fed. 687, cited by the bankrupt at page 12 of his brief, is likewise not in point. There, the bankrupt wrote a letter to the objecting creditor telling him that he did not have a statement of his financial condition as he had not

taken inventory for some time, but that he could only say that he was perfectly solvent, but due to extreme dullness of business, he had had very little business at all and that he expected to realize some money on a bankrupt stock which he had purchased. There was no representation that he had $12,500.00 in escrow. In fact, he even told the objecting creditor that business was poor. In reversing an Order denying his discharge, the Court of Appeals for the Fourth Circuit said:

> "Surely this letter, taken as a whole, fails to sustain the charge of deliberate and purposeful deception. Not only is there no definite representation as to assets or debts, or anything else, but the general assertion of solvency is so qualified by succeeding statements as to deprive it of any seriously misleading import. In short, we think the letter furnishes no evidence of that dishonest purpose to obtain credit which the law declares shall operate to prevent a discharge. * * * Moreover, the record does not show that appellee proved, or even attempted to prove, that it parted with its property on the faith of Rauch's letter and in reliance upon his statement that he was perfectly solvent, and certainly no presumption that such was the case arises from the facts now disclosed."

This case was determined in 1917, ten years before the 1926 amendment, which included "extension or renewal of credit," under the interdict imposed by Section 14 of the National Bankruptcy Act. In the case at bar, the witness, Goldberg, testified unequivocally that he believed the bankrupt's false statement regarding the $12,500.00 in escrow to be true [Tr. pp. 75, 97 and 98], and refrained from pressing the claim for immediate payment

[Tr. pp. 97, 107 and 108], and as a result of his forbearance found his company "holding the sack" in Mau's bankruptcy proceeding with a claim entirely unpaid [Tr. p. 83].

Much has been said in the bankrupt's brief with regard to the liberality which should be accorded a bankrupt in a right to his discharge. As an academic proposition, or as an abstract question of law, this may be true, but we know of no rule of law that requires the courts to be liberal with a *dishonest bankrupt*. In the *Matter of Merritt,* 28 F. 2d 679, the first case which this writer argued before this Court, the late Judge Gilbert closed his opinion affirming an Order denying a dishonest bankrupt's discharge in the following language:

> "Objections to a discharge need not be proved beyond reasonable doubt. A fair preponderance as in civil trials is sufficient. *In re* Garrity (C. C. A.), 247 F. 310. Said Judge Coxe, in *Re* Becker, 106 F. 54: 'A discharge is intended to relieve misfortune, but it must be misfortune coupled with absolute honesty. It is the reward which the law grants to the bankrupt who brings his entire property into court and lays it, without reservation, at the feet of his creditors."

In 1926, Section 14 was amended to shift the burden from the objecting creditors to the bankrupt when a *prima facie* case had been established and placing the burden on the bankrupt to show that he had not been guilty of any of the acts of omissions interdicted by Section c of the National Bankruptcy Act. See *Shanberg v. Saltzman,* 69 F. 2d 262; *Morton v. Snider,* 20 F. 2d 469; *Widder v. Seiff,* 94 F. 2d 6.

We might go still further and quote the language of the late Judge Cant of the District of Minnesota, in a bankruptcy case which was not reported in the Federal Reporter, but is found in the 14th Volume of the American Bankruptcy Reports (N .S.) at page 422:

> "When people like this bankrupt make up their minds either that they cannot or that they will not pay their debts, all that they need to do, when they invoke the provisions of our very indulgent law, is to go straightforward and see that they shall not come within the teeth of its provisions. Then no harm will come. They will often work out an outrageous result, but they are within the terms of the law. If they try any other course, they need not be surprised and should not complain if they find that they have pulled the house down upon their own heads.
>
> "This bankrupt has not offended more seriously than many others, but as fast as such matters come before the courts on records such as this, the disposition must be such as will serve to warn all that the right road is the best one to follow. The application for discharge should be denied."

In the *Matter of Breitling*, 133 Fed. 146, the bankrupt had omitted a bill owing him for $40.00 worth of lumber in drawing his schedules, had collected it shortly after bankruptcy and applied the money on costs and attorneys' fees. The District Court discharged him and on appeal, the Circuit Court of Appeals for the Seventh Circuit reversed the District Judge. Concluding its opinion, the Court said:

> "The amount involved, it is true, is small, but the design to conceal was deliberate and is clear. We are indisposed to give countenance in the slightest de-

gree to any act which shall withhold from creditors any part of the estate of a bankrupt which lawfully he should devote to the payment of his debts. The decree is reversed."

In the *Matter of Chris M. Jacobson, Bankrupt,* 9 F. 2d 139, the bankrupt, while drunk, had run over a small boy in Aberdeen, South Dakota, breaking his leg. Fearing suit, he recorded a transfer of 160 acres of land in Perkins County, South Dakota, to one A. W. Terriff. Judgment was entered against him in favor of the boy in the Circuit Court and Jacobson decided to go through bankruptcy. He procured a reconveyance of the land, recorded it, scheduled it in his schedules in voluntary bankruptcy, surrendered it to his trustee, and it was administered as assets in his estate. The Referee held that he had purged himself of any wrongdoing by procuring a reconveyance of the land before bankruptcy and scheduling it and therefore stood in *locus poenitentiae.* District Judge Elliott overruled the Referee's conclusions and denied the bankrupt's discharge by reason of the fact that he had kept this land in concealment during a part of the four months preceding the filing of the petition. We quote:

"In this particular case it appears without dispute that he transferred this property for the purpose prohibited in this statute, within the time named in the statute, and that an attachment had been levied upon the land as his property, and he was going to lose the property, and therefore, because it became apparent to him that his scheme to defraud was a failure, he brings the property so concealed into court, and asks the court to consider his privilege as

an honest debtor, and give him the benefits of the Bankruptcy Act in the discharge of his debts. In my judgment this is just such a situation as this provision of the law was intended to serve, and under the provision of this statute no debtor, who, within four months of the time of the filing of his petition, conceals his property with intent to hinder, delay, or defraud his creditors, can come into this court with the property he has concealed and say, in substance: 'Here is the property that I concealed with the intent and purpose prohibited by section 14c (4), and I now deem it to my best interests to file a petition in bankruptcy and to schedule the property, and therefore I am coming with clean hands and am entitled to my discharge.' The mere statement of the claim of such a right is not only repugnant to the plain provisions of the statute, but it is inconsistent with the well-settled principle of law that a discharge is by the terms of the statute expressly withheld from those whose conduct bring them within the provision of Section 14 of the Bankruptcy Act."

In the *Matter of Powell,* 22 F. 2d 239, the bankrupt was charged under Section 14b of the obtaining money or property on credit on a materially false statement in writing. The false statement in this case consisted of a chattel mortgage given by the bankrupts (husband and wife) on property which they did not own and knew they did not own at the time. In reply to the specious reasoning of the bankrupt's counsel that this did not constitute a materially false statement in writing as intended by the statute, the Court, after observing that he could not see why a false chattel mortgage, being in writing, did not fall within the definition, just as does a false statement of

assets generally, quoted from *In re Rea Brothers,* 251 Fed. 431, as follows:

> "We agreed with the learned District Judge that a 'materially false statement in writing' cannot be confined to a financial statement made by the bankrupt, or a statement of his financial condition, and that it may include any 'materially false statement in writing' made by the bankrupt for the purpose of obtaining money or property on credit and by which said property or money is obtained; *but we think such false statement should not be created by inference alone from acts of the bankrupt.*" (Italics ours.)

The Findings of the Special Master were reversed and the discharge denied.

In *Albinak v. Kuhn,* 149 F. 2d 108, another case where the bankrupt had represented that certain accounts receivable discounted by him were genuine, the Court of Appeals for the Sixth Circuit in affirming an Order Denying the Bankrupt's discharge, said:

> "The argument is made that these assignments, notwithstanding their covenants, do not constitute a financial statement, implying, of course, that a financial statement is a term of art and purports to be a complete statement of assets and liabilities by which the precise financial worth of the person making the statement can be determined. However, the statute does not use the phrase 'financial statement.' It refers to a false statement respecting financial condition, made or published 'in any manner whatsoever.' The argument is, we think, tenuous, that a written statement listing as assets accounts which have no existence whatsoever, running into many thousands of dollars and including practically all of the receivables of the assignor, are not statements respecting the maker's financial condition."

## Conclusion.

We could go on indefinitely citing cases involving denial of discharge of fraudulent bankrupts which indicate clearly that the so-called "liberality" surrounding questions of discharge, does not extend to dishonest bankrupts as distinguished from those whose bankruptcy is due to misfortune coupled with absolute honesty. Certainly, this bankrupt was anything but honest when he falsely represented in writing that he had $12,500.00 in an escrow which would be released shortly and if his creditor showed patience it would be paid in full and he and the creditor whom he deceived would be able to "resume business in the fall so that both of them could prosper" [Tr. p. 41]. The bankrupt did not say that he "expected" to have $12,500.00 put in escrow, or that he "expected" to raise $12,500.00 on his home of which $11,500.00 was to go to the bank, but stated as a positive fact that there was at that time $12,500.00 in escrow which would be released probably within three weeks. The bankrupt knew that statement was false and untrue and admits it, and how his counsel can picture him as an honest bankrupt worthy of the privilege of a discharge is beyond our comprehension. Possibly, our ideas of what constitutes honesty are warped or naive, but we still insist that the letter written by the bankrupt meets every test under Section 14c of the National Bankruptcy Act, namely, it was in writing, it misrepresented an asset of $12,500.00 which was non-existent. It was acted upon by the creditor to its detriment, and the bankrupt knew when

he made those representations that the representations were untrue. The bankrupt attempted throughout his testimony to convey the impression, although not directly so stating, that Ellis Wishnow, the creditor's representative, was responsible for his writing the letter in question. It is clearly evident upon a reading of the record that the bankrupt deceived Wishnow with the same line of talk that he incorporated into the written statement, and Wishnow merely suggested that he communicate that information to his superior, the Credit Manager. The act was the bankrupt's own and he should not now be absolved from the consequences of his own dishonesty.

We respectfully submit that the Order of the Referee and of the District Judge should be affirmed.

Dated this 9th day of August, 1950.

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